No. 80-202

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MICHAEL RODAK, JR., CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1979

AMERICAN EXPRESS COMPANY,
Petitioner,

v.

LOUIS R. KOERNER, SR.,
Respondent.

REPLY TO RESPONSE TO PETITION FOR WRIT OF CERTIORARI

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The Truth-in-Lending Act by its terms does not apply to business loans. The Fifth Circuit nonetheless ruled that the Act would be applicable where an individual assumes liability for business debts. The Fifth Circuit's opinion will radically alter business lending transactions and distort the availability and cost of funds. It also flies in the face of contrary rulings by the federal agency charged with responsibility for interpreting the Act.

Respondent in effect concedes that the ruling of the Fifth Circuit is wrong. Respondent admits that, under well-established principles of law, credit transactions having a business or commercial purpose are exempt from the Truth-in-Lending Act and that this exemption is not defeated because an individual assumes liability for business debts. Instead, Respondent argues only two points: (1) The Fifth Circuit's result can be supported by inventing a new rule denying the business credit exemption to business credit card programs; and (2) Since the

case can therefore be limited to credit cards, it lacks importance. Because Respondent's arguments are contrary to both the language and logic of the Fifth Circuit's opinion, and because Respondent does not quarrel with Petitioner's reading of the otherwise applicable legal principles, this case can be resolved simply. Certiorari should be granted and the decision below should be reversed.

I. The Fifth Circuit Has Effectively Repealed The "Business Purpose" Exemption From The Truth-in-Lending Act In All Cases Where An Individual Assumes Liability For Business Debts.

The Fifth Circuit specifically stated that it was ruling on only one issue: whether the business credit exemption provided by § 104 of the Truth-in-Lending Act is defeated because an individual assumes liability for the business debt. The Court said that it was *not* deciding whether the "business purpose" exemption was inapplicable to § 161 of the Act (the particular section assertedly violated by Petitioner). (App. A at 9a.) The Court noted that this question was "obviously difficult," and concluded that it "need not resolve that question, because a narrower ground for decision exists in this case" (App. A at 9a), i.e. whether the individual's assumption of liability to support a business loan makes the business exemption ineffective.

Respondent tries to read the lower court decision differently. Ignoring the express language quoted above, Respondent (while admitting that the Court of Appeals "did not decide" the issue, Response at 5-6) argues that § 104 is inapplicable to § 161 because of conflicts between the two sections, and that the existence of this conflict justifies the outcome reached by the lower court. Because of these assumed conflicts, Respondent argues that the lower court holding rests solely on an interpretation of § 161, that this section only applies to credit card companies and is therefore of little general importance, and that the decision is irrelevant to the broader range of credit trans-

actions potentially covered by § 104. This reasoning is flawed on all counts and cannot be accepted as a sound basis for denying the Petition.

First, the Fifth Circuit's decision cannot be "strictly limited to an interpretation of one section [§ 161] of the 1974 amendments to the Truth in Lending Act," as Respondent alleges. Response at 5. The Truth-in-Lending Act is structured in such a way that the § 104 exemption applies to all provisions of the Act, with the exception of three sections which are not involved in this case.[1] Unless there is a conflict between § 104 and the remaining provisions of the Act, the exemption contained in § 104 will be applicable to each of those provisions. Since the Fifth Circuit ruled in Respondent's favor, it must either have been interpreting the § 104 exemption (which would make the decision generally applicable to all Truth-in-Lending provisions) or it must have found that § 161 contains some provision implicitly repealing the § 104 exemption insofar as it would otherwise apply to that section. Since the Court expressly stated that it was *not* deciding "whether [§ 161] covers corporate transactions and transactions for business or commercial purposes" (App. A at 9a), its decision must logically be of general applicability.

Second, the Fifth Circuit could not properly have determined that there was a conflict between § 104 and § 161 because the express language of § 161 shows unambiguously that there is no conflict. Section 161 concerns billing errors in a "statement of the obligor's account in connection with an extension of *consumer credit.*" § 161(a), 15 U.S.C. § 1666(a) (1976) (emphasis added). The specific subsection of § 161 applicable to Respondent's claim below governs the closing of an "open-end *consumer*

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[1] Section 135 of the Act, 15 U.S.C. § 1645 (1976), provides that § 104 is not applicable to §§ 132, 133, and 134, 15 U.S.C. §§ 1642-44 (1976). Those sections concern issuance of unsolicited credit cards, limits of liability, and fraud.

credit plan" where the obligor has given the requisite notice of an alleged billing error. § 161(d), 15 U.S.C. § 1666(d) (1976) (emphasis added). Because the references to consumer credit serve to limit the operation of § 161 to non-business transactions,[2] § 161 cannot be read to preclude application of the business credit exemption contained in § 104.

Third, it is not true, as Respondent alleges, that § 161 (and other 1974 amendments) implicitly repealed § 104 with respect to those sections because of the difficulties in applying § 104 to credit cards. Respondent argues that because there is no "viable way" of distinguishing business from personal cards, Response at 9-10, the courts should interpret the Act to make § 104 inoperative, thereby extending the protections of the Truth-in-Lending Act to all individuals who are holders of credit cards. But the District Court had no difficulty articulating a "viable way" of distinguishing business from personal cards: one should simply determine, when a card is issued, whether "the reasonably anticipated predominant use" was for business or personal purposes. (Appendix C at 12c). The Federal Reserve Board staff has articulated

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[2] The Truth-in-Lending Act provides that:

> [t]he adjective "consumer," used with reference to a credit transaction, characterizes the transaction as one in which the party to whom credit is offered or extended is a natural person, and *the money, property, or services which are the subject of the transaction are primarily for personal, family, household, or agricultural purposes.*

§ 103(h), 15 U.S.C. § 1602(h) (emphasis added).

According to Regulation Z:

> "Consumer credit" means credit offered or extended to a natural person, in which *the money, property, or service which is the subject of the transaction is primarily for personal, family, household, or agricultural purposes.* "Consumer loan" is one type of "consumer credit."

12 C.F.R. § 226.2(p) (1980) (emphasis added).

a similar test. Public Information Letter No. 727, November 13, 1975, issued by Griffith L. Garwood (Appendix G at 3g-4g). In any event, the issue raised by this Petition is not whether the District Court's formulation is correct, or whether the test articulated by the Federal Reserve Board staff is correct, or even whether any other test which Respondent might propose is correct. The issue is whether the Court of Appeals can be allowed to avoid the need to formulate an appropriate test by creating, based on its own concept of equity, an exception from the otherwise applicable "business purpose" exemption for situations in which an individual is personally liable to a creditor. Since there is not, and cannot logically be, any basis for such a special rule, this Court should require the Court of Appeals to face the underlying issue.

Finally, respondent cites *American Airlines, Inc.* v. *Remis Industries, Inc.*, 494 F.2d 196 (2nd Cir. 1974) and *Credit Card Service Corp.* v. *FTC*, 495 F.2d 1004 (D.C. Cir. 1974) to suggest that § 104 does not apply to § 161. These cases are wholly inapposite. Because they dealt only with the 1970 amendments to the Truth-in-Lending Act, *not* the 1974 amendments to the Act which include § 161, they have no direct application here. Moreover, the reasoning of the two decisions has no bearing on resolution of the present case.

American Airlines and *Credit Card Service Corp.* together ruled that § 104 does not prevent the application § 133 of the Act and, by implication, the other 1970 amendments, 15 U.S.C. § 1642-44 (1976) (sections not at issue here) to business credit cards. These rulings—now codified at § 135 of the Act, 15 U.S.C. § 1645 (1976)—turned on an interpretation of the particular sections at issue. The cases found a conflict between § 104 and the 1970 amendments. Here, as we have previously noted, there is no basis for a finding of conflict between § 104

and § 161. Second, before *American Airlines* and *Credit Card Service Corp.* were heard, the Federal Reserve Board had determined that there was a conflict between § 104 and the 1970 amendments and had promulgated an amendment to Regulation Z providing that the business purpose exemption under § 104 would not apply to these provisions. 12 C.F.R. § 226.13(a)(4) (1973) (amended Nov. 2, 1972), now codified at § 226.2(m). Thus the two cases followed and confirmed prior administrative interpretations of the sections at issue. Here, the position of the Federal Reserve Board staff is that the 1974 Fair Credit Billing amendments, which include § 161, are subject to the § 104 business purpose exemption. Public Information Letter No. 1004, February 10, 1976, issued by D. Edwin Schmelzer (Appendix G at 7g-8g). Under these circumstances, *American Airlines* and *Credit Card Service Corp.* provide no support for Respondent's contentions.

II. Respondent Has Disregarded The Holding Of This Court In *Ford Motor Credit Co.* v. *Milhollin.*

Respondent has largely ignored Petitioner's argument that the court below was obliged under *Ford Motor Credit Co.* v. *Milhollin*, 100 S. Ct. 790 (1980), to follow applicable Federal Reserve Board staff opinions unless it finds those opinions "demonstrably irrational." As explained in the Petition, the Board staff has consistently taken the position that credit transactions for a business or commercial purpose are exempt from the coverage of the Act, even if an individual executes or guarantees the loan obligation. It has also determined that this exemption is applicable to that part of the Truth-in-Lending Act which contains § 161. Neither the Fifth Circuit nor Respondent have even attempted to apply the standard of review re-

quired under *Milhollin*. Instead, the Response, like the Fifth Circuit's opinion, relies on a strained reading of the definitions contained in Regulation Z to suggest that a contrary reading of the statute and regulations is more persuasive than the one adopted by the staff. But that is not the test. The Fifth Circuit did not purport to find that the staff's approach was "demonstrably irrational," and indeed it could not have done so in light of the language (cited above) specifically restricting § 161 to "consumer credit" transactions. *Supra* at 3-4. Under *Milhollin*, the decision below cannot stand.

III. Respondent, By Misconstruing The Scope Of The Lower Court's Decision, Has Misconceived Its Impact On Credit For Business Enterprises.

Respondent argues that the decision of the Court of Appeals deals only with credit cards and is therefore unimportant. Even if the decision had been so limited, respondent is seriously mistaken in his belief that the impact is minimal. Business credit cards are an efficient and convenient means of extending credit to both large and small enterprises. Their use is widespread: there are millions of cards issued under a wide variety of business programs. The opinion below will have significant effects on both the users and issuers of such cards.

In any event, the Court of Appeals did not limit its decision to credit cards. The court explicitly elected to establish a generic rule: it held that the § 104 business purpose exemption will not apply where an individual assumes liability for debts incurred. This means that in every instance where the individual assumes liability, the creditor will be subject to the Truth-in-Lending Act. Because of the importance of personal guarantees or other personal liability in business credit transactions, the

court's decision has serious consequences for all business credit, and this Court should grant the Petition to correct the error made by the Fifth Circuit.

Respectfully submitted,

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